Blended finance and the water sector –
four risks to consider

Eurodad welcomes the Organisation for Economic Cooperation and Development’s (OECD’s) actions to open up debate on blended finance and the water sector.

We agree that financing for safe drinking water, sanitation and hygiene is a crucial issue. Access to safe drinking water and sanitation is a human right, and is fundamental to the enjoyment of other rights such as the highest attainable standard of health. Under Sustainable Development Goal 6, the global community has committed that, by 2030, all people will have universal and equitable access to safe and affordable drinking water (target 6.1) and access to adequate and equitable sanitation and hygiene, including an end to open defecation, with “special attention to the needs of women and girls and those in vulnerable situations” (target 6.2). Yet in 2015 more than 840 million people worldwide did not have access to a basic drinking water service, and 2.3 billion people lacked a basic sanitation service. A World Bank study estimated that the capital costs alone of meeting SDG targets 6.1 and 6.2 would be around 114 billion USD per year.

How best to source this finance is an urgent question. This briefing sets out four risks that we hope will be thoroughly considered in the forthcoming discussions. Wherever relevant it draws closely on the OECD Development Assistance Committee’s (DAC’s) Blended Finance Principles, which were agreed in October 2017 as a framework “to ensure blended finance meets accepted quality standards and achieves impact, based on a development rationale”.

Risk 1: leaving people and countries behind

Enjoyment of the right to safe drinking water and sanitation is subject to severe geographic and demographic inequalities. For example: in 2015, less than a third of the population of Least Developed Countries had access to a basic sanitation service, with the proportion being even lower in rural areas. Low-income segments of the population can experience extreme disparities in access, and marginalised groups such as women with disabilities tend to be particularly hard hit. Reaching these populations who cannot currently access safe drinking water and sanitation is key to meeting SDG 6. This requires building and – crucially - operating and maintaining infrastructure in hard-to-access geographies, and providing services at low or no cost to marginalised populations. However, such interventions are “the very projects which are least likely to attract private investors”, as there is little prospect of short-term commercial returns. The Overseas Development Institute recently argued that in many of the poorest countries, often the “fundamental economics are not right” for blending, as infrastructure projects lack secure streams of positive cash flows.

The UN Inter-Agency Task Force on Financing for Development’s 2018 report found that “the use of private finance is more challenging in areas where equity considerations and large financing gaps reduce profit prospects — such as water.”

In contrast, public finance is not subject to the same pressure to make a profit – one of the reasons why, historically, public sources have been the “mainstay” of water and sanitation infrastructure development worldwide. In making the case for blending, it is often stated that public finance, and other ‘traditional’ sources of finance, are not sufficient to meet the SDGs’ infrastructure financing needs. However, as a recent Eurodad briefing argued, the evidence does not bear this assertion out.

Solutions for mobilising significant sums of additional public finance are well known - such as clamping down on tax dodging, and meeting ODA commitments. Too much focus on mobilising private finance risks detracting attention from the urgent challenge of putting these public financing solutions into practice.

Risk 2: undermining local ownership of development priorities

The OECD DAC Blended Finance Principles state that blended finance should “support local development priorities” (Principle 3a). This draws on the established development cooperation principle that development priorities must be owned by countries in the Global South, and partnerships for development should put these countries in the lead. Yet in practice the complex governance of blending risks eroding local ownership and accountability, as past research has found. What is more, blended finance has at times been explicitly used as a tool to advance donors’ own policy reform objectives. An evaluation of European Union blending between 2007 and 2014 said that one motivation for blending was that the recipient government would be “more easily persuaded to adopt the reforms or conditions attached to the loan (e.g. increase in tariffs) since there is a substantial subsidy element”. The evaluation gives the example of a water and sanitation project in Armenia.
Conclusion: the need for caution

Financing universal access to safe water and sanitation is imperative for fulfilling human rights and achieving the SDGs. But, as this briefing has argued, mobilising finance carries risks as well as opportunities. In the case of blended finance, these risks include:

- Diverting attention from the fundamental issue of how to increase and improve public investment in water and sanitation services that reach the most marginalised people.
- Undermining local ownership of development priorities.
- Harmful consequences including human rights abuses, tax avoidance, and unsustainable debt burdens.
- Diverting scarce development finance from other vital uses, without sufficient evidence of impact.

In the absence of compelling evidence of effective mitigations for these risks, we reiterate our position that any moves to scale up blended finance are premature.

References

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